

Software Working Group Meeting Minutes

March 21, 2023, 2:00 PM to 3:00 PM EST

Video Conference (Zoom)

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Attendance

Mr. Williams, FASAB senior analyst, conducted the meeting via Zoom. Approximately 20 people attended the meeting.

Introduction

The task force meeting convened around 2:00 PM EST.

Welcome

Mr. Williams welcomed and thanked everyone for their previous comments on the cost-benefit analysis of reporting options for cloud-service arrangements. He stated that the information they provided was essential for the Board to weigh the user benefits and preparer burdens of each reporting option. He also stated that he intended the meeting as a roundtable discussion and encouraged participants to speak up anytime with questions or comments.

Project Recap

Mr. Williams then provided a recap on the progress of the software technology project. He stated that during the August and October 2022 meetings, staff presented the primary ways that federal entities acquire cloud services and the Board deliberated whether cloud-service arrangements could meet the SFFAC 5 asset concepts and whether they were more like right-to-use assets or service contracts.

Mr. Williams stated that Board members appeared to have differing opinions on these issues and that the cost-benefit analysis of the reporting options would ultimately drive which direction the Board takes.

Meeting Objectives

Mr. Williams explained that the purpose of the meeting was to discuss further the potential benefits and preparer burdens associated with each reporting option in the cost-benefit analysis. He mentioned that he had spoken with and planned to speak further with non-preparer stakeholders who expressed an interest in federal cloud information, including representatives from academia, IT private industry, auditors from

GAO Information Technology Cybersecurity, and staff from the Senate Committee on Homeland Security and Government Affairs.

Cost-benefit Analysis

Mr. Williams then provided an overview of the cost-benefit analysis and summary of working group comments. He addressed each reporting option and invited open dialogue.

Reporting Option 1 – Asset/Liability Recognition

Mr. Williams stated that this reporting option would look similar to both SFFAS 54, *Leases: An Amendment of Statement of Federal Financial Accounting Standards (SFFAS) 5, Accounting for Liabilities of the Federal Government, and SFFAS 6, Accounting for Property, Plant, and Equipment* and GASB Statement No. 96, *Subscription-Based Information Technology Arrangements*. Essentially, this reporting option would require preparers to recognize multi-year cloud-service commitments as a right-to-use asset with a corresponding liability for future payment on the balance sheet. Preparers would also have to measure the asset and liability at net present value and amortize the asset over its useful life.

Mr. Williams expressed some concern with this reporting option. He indicated that initially, the Board wanted to consider implementing similar reporting requirements to GASB 96 for cloud-service arrangements in the federal space. However, after extensive research, it does not appear that this reporting framework cleanly fits with the current federal cloud environment. Federal entities appear to acquire cloud-services in many ways, including in pay-as-you-go manner based on variable usage. These types of arrangements would not fit the scope of this reporting option and be left out of reporting.

Additionally, Mr. Williams stated that this reporting option in theory would improve transparency of federal net position. However, the amounts of the multi-year cloud-service commitments would be relatively minor compared to other assets and would likely not visibly affect balance sheet presentation. Furthermore, Mr. Williams indicated that other stakeholders had expressed interest in multi-year cloud-service commitment information, but did not particularly express an interest in the information presented as a right-to-use asset on the balance sheet.

Mr. Williams acknowledged all of the systems changes and resource needs that preparers would need to implement this reporting option. In summary, this reporting option appeared to present with the greatest preparer burden with minimal benefits without further accompanying information.

One working group member reiterated concern with cloud-service arrangements not meeting the current FASAB asset and liability concepts because arrangements often include a bundle of different deliverables and services. Mr. Williams acknowledged this concern and the fact that this reporting option would require asset recognition. He stated that the Board had previously deliberated this issue multiple times and appeared

to currently have differing opinions on whether multi-year cloud-service commitments were right-to-use assets or service contracts.

Reporting Option 2 – Commitment Disclosures

Mr. Williams then explained that reporting option 2 would require preparers to disclose the dollar amount of multi-year cloud-service commitments in financial statement notes. He reiterated that some non-preparer stakeholders had expressed interest in this kind of information.

One working group member understood that there might be a niche interest for cloud commitment information but that reporting them while not reporting any other types of commitments could mislead users of the general financial report. For example, there are many other categories of commitments in the federal environment, such as construction contracts, that would be more significant than cloud-service commitments. Mr. Williams acknowledged this concern and stated he would include the point in the Board material.

Reporting Option 3 – Expense Disclosures

Mr. Williams then explained that reporting option 3 would require preparers to disclose all cloud-service annual expenditures in financial statement notes. The disclosures could include present and prior fiscal year expenditures. Mr. Williams stated that the positive with this reporting option versus the previous two is that the information would include all cloud-service expenditures, whether acquired via multi-year commitment or pay-as-you-go. He reiterated that some non-preparer stakeholders had expressed interest in this kind of information.

One working group member expressed concerns similar to commitments. That is that annual cloud-service expenditures are very small relative to total annual operating expenditures and other types of expenditures would be more significant but do not require disclosure.

Mr. Williams agreed that the total annual cloud-service expenditures are very small relative to total operational expenses. However, he stated that annual cloud-service expenditures are very significant relative to current capitalized internal use software (IUS) assets. For example, in FY 21 the federal government spent approximately \$11 billion for cloud services and capitalized amortized only \$3 billion for capitalized IUS. Additionally, IUS capitalization appears to be trending down, with only \$4.5 billion capitalized in FY 21. This indicates that the federal government is spending more on cloud services than relying on internal use software for IT operational needs. Without the cloud expenditure information, the current IT cost picture is incomplete.

One working group member stated that the downward trend in capitalized IUS could also be attributed to other factors, such as legacy systems and more agile IUS development methods. Mr. Williams acknowledged that other factors could affect IUS

capitalization but that it was clear that cloud spending in the federal environment has grown tremendously.

Reporting Option 4 – Expense Recognition Only

Mr. Williams then explained that reporting option 4 would only require preparers to recognize cloud-service arrangement costs as general operating expenditures without any further reporting requirements, which is the status quo among federal entities. He stated that while this option requires no further reporting requirements, it is possible that the Board could decide it is the best reporting option after weighing costs and benefits.

Final Thoughts

Mr. Williams indicated that several working group members preferred reporting option 4, a few preferred reporting options 2 and 3, and one working group member preferred reporting option one with caveats. He stated that working group members had expressed that the first three reporting options would all require new systems and process changes to implement but that there seemed to be a consensus that option 1 would be most burdensome to implement.

Regarding options 2 and 4, a couple of working group members questioned if the general financial report would be the best format for tracking cloud spending and commitments. One working group member suggested that the information would still benefit users and be less burdensome to preparers if included in required supplementary information or other information. Another working group member suggested that cloud cost information may be more useful if expressed in other terms, such as usage or data, and may be more appropriate presented as forward looking information in the MD&A.

Mr. Williams acknowledged those concerns and points. However, he stated that financial reporting also improves accountability of resources. He referenced a 2019 GAO audit report that found that federal entities have trouble tracking cloud spending and therefore miss savings opportunities. He agreed however, that accountability comes with costs and that it is ultimately important for the Board to properly weigh the costs and benefits of reporting.

Next steps

Mr. Williams encouraged everyone to continue to provide him information and comments as he finalized the material for the Board meeting in April. He reiterated that he would do his best to ensure that he communicated working group members' thoughts and concerns with each reporting option.

Conclusion

Mr. Williams concluded by thanking everyone again for all of their time and efforts. He reiterated the importance of their participation in the working group for helping the Board make informed financial reporting decisions for cloud-service arrangements.

The meeting concluded at approximately 2:50 PM EST.